No. 22,387

IN THE

United States
Court of Appeals

FOR THE NINTH CIRCUIT

WESTERN TERMINAL COMPANY, *Appellant*

v.

UNITED STATES OF AMERICA, *Appellee*

On Appeal from the Judgment of the United States District Court for the Eastern District of Washington

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BRIEF FOR THE APPELLEE

MITCHELL ROGOVIN
Assistant Attorney General.

LEE A. JACKSON,
WILLIAM FRIEDLANDER,
JEANINE JACOBS,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

Of Counsel:
SMITHMOORE P. MYERS,
United States Attorney.

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OPINION BELOW

The findings of fact and conclusions of law (I-R. 24-28) have not yet been officially reported.

JURISDICTION

This appeal involves federal income taxes for the year 1960. On June 3, 1964, the taxpayer paid a deficiency in its income tax for the taxable year 1960 in the amount of $203,222.05 (plus interest). (I-R. 11.)

Taxpayer filed claim for refund of this sum on January 29, 1965, which claim was denied April 2, 1965. (I-R. 11.) Within the time provided by Section 6532 of the Internal Revenue Code of 1954, on March 18, 1966, the taxpayer brought the action in the District Court for recovery of the $203,222.05 together with interest as provided by law. (I-R. 1-3.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1346. The judgment of the District Court was entered on September 5, 1967, awarding the taxpayer the principal amount of $64,313.21. (I-R. 29.) Within 60 days thereafter, on September 26, 1967, the taxpayer filed a notice of appeal. (I-R. 30.) Jurisdiction is conferred on this Court by 28 U.S.C., Section 1291.

QUESTION PRESENTED

Whether the District Court clearly erred in finding, as a factual matter, that the useful life of taxpayer's fuel storage facility was 20 years (as contended by the Government) and not 5 years (as contended by the taxpayer).

STATUTE AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra*.

STATEMENT

The facts, as found by the District Court (I-R. 24-27), many of which were admitted in the pretrial conference order (I-R. 10-13), are as follows:

The taxpayer is a corporation organized and existing under the laws of the State of Washington, with its principal business address at 220 North Haven Street, Spokane. Washington. (I-R. 24.)

The taxpayer was organized on February 11, 1959, for the purpose of bidding on a contract with the United States Government, for the construction and operation of a fuel storage facility to be located adjacent to the Grand Forks North Dakota Air Base. (I-R. 24.)

On April 22, 1959, the taxpayer was awarded a contract for storing and handling Government-owned petroleum products at Grand Forks, North Dakota, which contract was modified as to size by a subsequent contract dated May 8, 1959. This contract was for a period of five years with three options to renew for additional five-year periods. (I-R. 25.) Under it, taxpayer was to construct the storage facility and to be reimbursed for the cost thereof by payments from the Government over the first five-year period.

At the end of any of the four five-year periods the Government had a right to purchase the storage facility by paying the following amounts (I-R. 25):

At the end of the fifth year	$937,500.00
At the end of the first renewal period	800,000.00
At the end of the second renewal period	600,000.00
At the end of the third renewal period	375,000.00

The contract also provided that the Government could terminate on 30 days notice by paying 30% of the unexpired use charges for the period. Upon termination the Government had the option to purchase for certain specified amounts. (I-R. 25.)

The contract, Department of Defense negotiated Contract No. A.S.P.-17894, was in the amount of $3,186,000, and was based upon the following estimates of cost, operating expenses and profit (I-R. 25):

Construction Cost	$1,875,000
Termination settlement	162,000
Operating Costs (5 years at $124,500 a year)	622,500
Interest on construction	326,625
Total estimated Costs	$2,986,125
Profit	199,875
Firm 5-year price	$3,186,000

The total price for the three five-year renewal periods totaled $1,984,500 and included estimated costs of operation and maintenance. (I-R. 25.)

Between April 27, 1959, and September 1, 1959, taxpayer constructed a storage facility near Grand Forks, North Dakota, for receiving, storing and distributing petroleum products to the Grand Forks Air Force Base, which is located some 15 miles from the site of the storage facility. (I-R. 26.)

The storage facility constituted property used in the taxpayer's trade or business of a type subject to an allowance for depreciation under the provisions of Section 167 of the Internal Revenue Code of 1954. (I-R. 26.)

The taxpayer's cost for the storage facility was as follows (I-R. 26):

Land	$ 35,935.10
Terminal facilities	794,026.66
Pipelines, off site	294,505.60
	$1,124,467.36

The cost of the depreciable assets was $1,088,532.26 (terminal facilities plus pipelines). (I-R. 26.)

Taxpayer, at all times during the year 1960, was the owner of the fuel storage facility. (I-R. 26.)

As of January 1, 1960, the depreciable assets included in taxpayer's fuel storage facility had an adjusted basis of $1,034,264.88. (I-R. 26.)

On January 13, 1961, the taxpayer sold the storage facility for $1,934,250. (I-R. 26.)

The Government exercised its option to renew its storage contract for the second five-year period which began October 1, 1964. (I-R. 26.)

The storage facility in question has a physical life of at least 20 years. (I-R. 26.)

Taxpayer made a timely election to compute the depreciation deduction to be allowed to it on the declining method using a rate twice that allowed by the straight line method. (I-R. 26.)

In computing the amount of depreciation to be allowed taxpayer for its taxable years 1959 and 1960, taxpayer estimated that said storage facility had a useful life of five years. Taxpayer made no estimate of the salvage value of the depreciable assets on its returns for those years. The Government contends that the storage facility has a useful life of 20 years. (I-R. 27.)

The storage facility will have no commercial use upon termination of use by the United States Air Force. Its only value will be as scrap value. (I-R. 27.)

The Grand Forks Air Base was completed in 1960 and the storage facility was constructed to supply the Air Base. The Grand Forks Air Base is expected to be in use for many years to come with a present projection of slightly increased use. (I-R. 27.)

In prior dealings with the Government the taxpayer had been the low bidder on the first five-year period of a similar contract for another project but had not received the contract since it was not the low bidder on the full 20-year period. On the bidding on the contract here in question the taxpayer was not the low bidder on the first five-year period but received

the contract as a result of being the low bidder on the 20-year period. In order to be the low bidder on the 20-year period the taxpayer submitted a revised bid which was substantially lower than its original bid. (I-R. 27.)

During the negotiations surrounding the renewal of the contract for the first option period the taxpayer offered to reduce the renewal price if the Government would relinquish its final two options to renew. The Government refused this offer. (I-R. 27.)

On the basis of the foregoing, the District Court concluded (I-R. 27-28):

> Using hindsight, it is clear that the five year useful life claimed by the plaintiff was unrealistic. All the testimony and evidence indicated that the storage facility would be used for at least 20 years.
>
> The storage facility had a useful life of 20 years for purposes of computing the depreciation deduction under Section 167 of the Internal Revenue Code of 1954.

SUMMARY OF ARGUMENT

The question raised by this appeal is whether the taxpayer was entitled, in the second year (1960) of use of a storage facility built in 1959 under a Government defense contract for receiving, storing and distributing petroleum products, to a depreciation deduction for his fuel storage facility based on a 20-year

useful life (as contended by the Government, and found by the District Court) or a five-year useful life (as contended by the taxpayer). The contract provided that the Government would use taxpayer's facility for storage of Government owned fuel for a term of five years with options on the part of the Government to renew the contract for three successive five-year periods at fixed option prices. It was stipulated that the storage facility in question has a physical life of at least 20 years; it is agreed that whether its useful life was 20 years, or some lesser period, depended entirely upon the portion of the 20-year option which the Government would eventually exercise. The evidence clearly established that when the contract was awarded, it was awarded on a predicted use by the Air Force of the full 20 years. Thus, bids that would have granted the Air Force more favorable terms than taxpayer's bid in the initial five-year period at the price of accepting less favorable terms over the full 20-year period were rejected in favor of taxpayer's bid.

It was the taxpayer's burden to establish by a preponderance of the evidence that the conditions known to exist at the end of 1960, the tax year in question, would reflect a reasonable certainty that the facility would be used for some specific period less than the 20-year term. This is consistent with the very basic precepts of depreciation accounting which seek to make a meaningful allocation of cost to the tax period benefited by the use of the asset.

Taxpayer wholly failed to meet this burden. He relied essentially on (1) the very fact of non-certainty itself and the conservative financing arrangements made by him in keeping with that non-certainty and (2) the uncorroborated and vague assertions that the B-52's which the facility was intended to service, would be phased out.

But, as this Court has held, the mere possibility of non-renewal does not establish with the required reasonable certainty that the contract will not run for the full 20-year period, and this will not support a foreshortened useful life. Nor does business acumen or prudence have any bearing insofar as we are concerned with estimating useful life for tax depreciation purposes. Moreover, the taxpayer's conjecture neither took account of servicing existing B-52's and/or other successor bomber aircraft, nor did it provide any basis in fact for a necessary finding that the asserted phasing out would reach such a stage at any given point within the 20-year period as to bring about discontinuance of the use of the facility.

In short, the taxpayer has failed to show a reasonable certainty of non-renewal or that there is any other basis for adopting less than the 20-year useful life used by the Commissioner and found by the District Court.

ARGUMENT

THE DISTRICT COURT CORRECTLY HELD THAT TAXPAYER WAS ENTITLED TO A DEPRECIATION DEDUCTION FOR ITS FUEL STORAGE FACILITIES BASED ON A TWENTY-YEAR USEFUL LIFE AS CONTENDED BY THE GOVERNMENT, RATHER THAN ON A FIVE-YEAR USEFUL LIFE AS CONTENDED BY THE TAXPAYER

Section 167(a) of the Internal Revenue Code of 1954, Appendix, *infra,* allows a depreciation deduction for the exhaustion, wear and tear, including a reasonable allowance for obsolescence of property used in a trade or business.

This case deals with a storage facility built under a Government defense contract for receiving, storing and distributing petroleum products to the Grand Forks Air Force Base which is located some fifteen miles from the site of the storage facility. The contract provided that the Government would use taxpayer's facilities for storage of Government owned fuel for a term of five years with options on the part of the Government to renew the contract for three successive five-year periods at fixed option prices. (I-R. 25-26.) The

sole question raised by this appeal is the useful life of this facility for purposes of tax depreciation deduction under Section 167(a).[1] The District Court found that it is twenty years. The taxpayer, who unsuccessfully urged a five-year period at trial (II-R. 9-10), appeals.

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[1]Any reasonable and consistently applied method of computing depreciation may be used or continued in use under Section 167 including the double declining balance method used by this taxpayer. Section 167(b)(2), Appendix, *infra*. Under the declining balance method a uniform rate is applied each year to the unrecovered cost or other basis of the property. Such rate determined under Section 167(b)(2) shall not exceed twice the appropriate straight line rate computed without adjustment for salvage. See Sec. 1.167(b)-2, Treasury Regulations on Income Tax, Appendix, *infra*.

While the governing statute has at no time defined the term "useful life" (*Massey Motors* v. *United States,* 364 U.S. 92, 97), Treasury Regulations on Income Tax (1954 Code), Section 1.167(a)-1(b), Appendix, *infra,* sets forth relevant considerations for determining that life as follows:[2]

> (b) *Useful life.* For the purpose of section 167 the estimated useful life of an asset is not necessarily the useful life inherent in the asset but is the period over which the asset may reasonably be expected to be useful to the taxpayer in his trade or business or in the production of his income. This period shall be determined by reference to his experience with similar property taking into account present conditions and probable future developments. Some of the factors to be considered in determining this period are (1) wear and tear and decay or decline from natural causes, (2) the normal progress of the art, economic changes, inventions, and current

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[2]The term "useful life" was first inserted in the pertinent statutory provision in the Congressional enactment to the 1954 Code Section 167(b)(4). The accompanying House Report to the bill, H. Rep. No. 1337, 83d Cong., 2d Sess., p. 22 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4046-4047) stated:

> Depreciation allowances are the method by which the capital invested in an asset is recovered tax-free over the years it is used in a business. The annual deduction is computed by spreading the cost of the property over its estimated useful life.

> developments within the industry and the taxpayer's trade or business, (3) the climatic and other local conditions peculiar to the taxpayer's trade or business, and (4) the taxpayer's policy as to repairs, renewals, and replacements. Salvage value is not a factor for the purpose of determining useful life. If the taxpayer's experience is inadequate, the general experience in the industry may be used until such time as the taxpayer's own experience forms an adequate basis for making the determination. The estimated remaining useful life may be subject to modification by reason of conditions known to exist at the end of the taxable year and shall be redetermined when necessary regardless of the method of computing depreciation. However, estimated remaining useful life shall be redetermined only when the change in the useful life is significant and there is a clear and convincing basis for the redetermination. * * *

It is settled that "the primary purpose of depreciation accounting [is] to further the integrity of periodic income statements by making a meaningful allocation of the cost entailed in the use * * * of the asset to the periods to which it contributes." *Massey Motors* v. *United States, supra,* p. 104. In effect, the purpose of depreciation accounting is "to approximate and reflect the financial consequences of the subtle effects of time and use on the value of his capital assets." *Detroit Edison Co.* v. *Commissioner,* 319 U.S. 98, 101. See also *Virginian Hotel Co.* v. *Helvering,* 319 U.S. 523, 526, 528.

It is the responsibility of the taxpayer to establish

the reasonableness of the deductions for depreciation claimed. Treasury Regulations on Income Tax (1954 Code), Sec. 1.167(b)-0, Appendix, *infra*.

The parties stipulated (I-R. 13) and the District Court found (I-R. 26) that the facility in question had a physical life of at least 20 years.[3] It was the taxpayer's burden to show as a factual matter by a preponderance of the evidence that, on the basis of facts existing as of the end of 1960, it was reasonably certain the terminal would be used for less than 20 years, i.e., that the contract in question would not

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[3]It was further stipulated and found (II-R. 100, I-R. 27) that the storage facility will have no commercial use upon termination of use by the United States Air Force.

be renewed over that period.[4] *Westinghouse Broadcasting Co.* v. *Commissioner,* 309 F. 2d 279 (C.A. 3d), certiorari denied, 372 U.S. 935; *Lassen Lumber & Box Co.* v. *Blair,* 27 F. 2d 17 (C.A. 9th); *Richmond Television Corp.* v. *United States,* 354 F. 2d 410 (C.A. 4th); *Gordon Lubricating Co.* v. *Commissioner,* decided May 18, 1965, 24 T.C.M. 697. Indefinite expectations *(Dunn* v. *Commissioner,* 42 T.C. 490; *Gordon Lubricating Co.* v. *Commissioner, supra)* or the taxpayer's unsupported opinion; *Bullock* v. *Commissioner,* 26 T.C. 276, 278-282, affirmed *per curiam,* 253 F. 2d 715 (C.A. 2d) is not enough to meet his

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[4]The District Court, in rejecting taxpayer's claim to a right to use a five-year useful life, in part took into account facts existing at the time of trial (e.g., the then continuing operation of the facility and storage contract) which it referred to as "hindsight." Taxpayer here urges that the consideration of such circumstances was improper. For purposes of this appeal, the Government will not urge the propriety of the use of any evidence not known to, or reasonably knowable by, taxpayer as of the end of the year 1960—the tax year here in issue. Rather we will show that the taxpayer has failed to adduce any evidence capable of meeting its burden of showing that, as of the end of 1960, there was a reasonable certainty that the useful life of the storage facilities would end in less than the twenty years determined by the District Director and that, for this reason, the court below could not, in any event, properly have made any finding of useful life other than the one here under appeal.

burden. The facts presented by the taxpayer in attempted discharge of his burden must be such as to demonstrate grounds for a reasonable certainty that the useful life of the property would terminate at the time estimated by him and used in his depreciation schedule. E.g., *Lassen Lumber & Box Co.* v. *Blair, supra; Gordon Lubricating Co.* v. *Commissioner, supra.* Moreover, the issue before the trial court is not, as taxpayer seems to suggest (Br. 10-11), whether it was in fact subjectively persuaded (for whatever reasons) that five years was the period over which the facility should be depreciated but whether, on the facts presented to the trial court, one using the proper legal test governing depreciation deductions would reasonably have been justified in using that period. *Bullock* v. *Commissioner, supra; Lassen Lumber & Box Co.* v. *Blair, supra.* Compare *Richmond Television Corp.* v. *United States, supra.* The District Court rightly found (I-R. 27) "All the testimony and evidence indicated that the storage facility would be used for at least 20 years," and, we submit, fixing the focus on December, 1960 (Br. 21-38), it is clear that there is no basis in the record to support a reasonable certainty that a five-year period was the more likely useful life.

The primary and controlling evidence which established that, as of the time the contract was entered into, the probabilities involved here indicated a useful life for the taxpayer's facilities of 20 years, is

the contract itself and the conditions surrounding the award of the contract. First the contract clearly was awarded on a 20-year basis. It should be noted that the contract was awarded to the taxpayer on the basis of an over-all low 20-year bid, despite the fact that it was not low bidder for the initial five-year period (I-R. 27; II-R. 132-133, 135-136, 148-149, 151-152)[5] —a fact which, based on a necessary assumption of rational behavior by the Government representatives, clearly reflects their then belief that renewal was more likely than otherwise. Second, the District Court noted that the taxpayer itself was willing to take, had wanted and had gone after the contract on the basis of 20 years (I-R. 27, II-R. 67, 120, 123), knowing that it had lost a previous contract because, though the low bidder on the first five-year period, it had not been the 20-year low bidder (II-R. 63, 68, 120, 123). To achieve this end it even submitted a revised

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[5]For example, see the schedule below comparing the taxpayer's bid for the first five-year period and that for the full 20-year period with those of two other bidders, Boyington and U.S. Service (for source of figures, see Taxpayer's Exhibit 13):

	Taxpayer	*Boyington*	*U.S. Service*
First five-year period	$3,584,500	$3,574,644.30	$3,349,986.60
Full 20-year period	$5,594,500	$6,790,644.30	$6,565,986.60

bid lower than its original bid. (I-R. 27.) Third, the options to renew were all on terms favorable to the Government. (II-R. 81-82.)[6] Nothing is shown to have happened between May of 1959 when the contract was awarded and the close of 1960 to alter the controlling effect of this evidence or to the taxpayer's contention that less than a 20-year use was indicated. *Westinghouse Broadcasting Co.* v. *Commissioner,* 309 F. 2d 279 (C.A. 3d), certiorari denied, 372 U.S. 935; *Richmond Television Corp.* v. *United States,* 354 F. 2d 410 (C.A. 4th).

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[6]The contract was limited to an initial five-year lease period because Section 416 of the Act of August 3, 1956, P. L. 968, 70 Stat. 991 (now 10 U.S.C. 2388) enacted specifically to handle facilities such as the one in question imposed the following restriction (Br. 12):

> The Secretaries of the military departments are authorized to contract for the storage, handling, and distribution of liquid fuels for periods not exceeding five years, with option to renew for additional periods not exceeding five years, for a total not to exceed twenty years. This authority is limited to facilities which conform to the criteria prescribed by the Secretary of Defense for protection, including dispersal and also are included in a program approved by the Secretary of Defense for the protection of petroleum facilities. * * *

For further legislative history see taxpayer's brief, pp. 12-15.

On brief, taxpayer relies primarily upon two types of circumstances, allegedly existing and known in 1960, to support his contention that he has met his burden of showing a reasonable certainty that a five-year, rather than 20-year, useful life was proper. First, taxpayer cites (Br. 10-11) the fact that the binding contract was only for a five-year lease period and that there was no certainty (i.e., legal commitment) for renewal. But, as the Regulations (see Treasury Regulations on Income Tax, Secs. 1.167(a)-1(b) and 1.167(b)-0, Appendix, *infra*) clearly state, the estimate of useful life is not predicated upon, or limited to, legal or factual certainties but upon what, in the light of all the relevant facts, is the most likely period of use in taxpayer's business. See *Massey Motors, supra; United States* v. *Ludey,* 274 U.S. 295; *Lassen Lumber & Box Co.* v. *Blair, supra,* p. 19. Thus, as taxpayer itself recognizes (Br. 30), the question at bar is "whether it was more probable than not that the Government would renew its contract." The District Court held that the taxpayer having the burden of proof on the point, had failed to establish with the requisite certainty that it would not be renewed. The same comments apply to taxpayer's related references to (Br. 11) the bases upon which it had submitted its financial statements to its banker; to the period over which the bank had re-

quired repayment of the loan (Br. 11);[7] to the Government's right to terminate even before the end of the committed five-year period (Br. 16); and to the fact (Br. 16-17) that, as a prudent businessman, it had protected itself against nonrenewal by insisting upon reimbursement of its construction costs over the committed five-year period. None of these things control the useful life for depreciation purposes where the taxpayer fails to show that the probabilities were clearly for nonrenewal. Obviously, taxpayer and his bank would protect themselves against even a mere possibility of nonrenewal but such a prospect would not support use of a useful life limited to the first five-year lease period. See the relevant comments of this Court in *Lassen Lumber & Box Co.* v. *Blair, supra,* p. 19. Consequently, the fact that taxpayer did these things, whatever his motivation, is probative of nothing in so far as estimating useful life for tax depreciation purposes is concerned.

Second, taxpayer makes much (Br. 11) of certain rumors and conjectures which had come to his attention with respect to the phasing out of manned bombers. But, these were, as we will show, *infra,* nothing more than that. The record shows (II-R. 204

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[7]In any event, by the impartial testimony of the bank's vice-president, these financing arrangements were standard procedure. (II-R. 229.)

et seq.), up through the taxable year here in issue, there had been no building of the Minutemen missiles by Boeing at the Grand Forks Air Force Base, nor evidence of discontinuance of the manned bombers. As taxpayer's president himself testified (II-R. 198), he had been told by the commander of the base, in 1960, that there was anticipated additional use by wing bombers. The true nature of the information available to the taxpayer respecting the anticipated influx of Minutemen missiles is seen in the following testimony of its president (II-R. 212-215):

A I think they will quit flying these manned bombers and they will cease to use our services very shortly, war or no war.

Q And can you tell me, what is the basis for this opinion?

A These planes are obsolete, they were designed nearly fifteen years ago, and it is not much of an airplane anymore.

Q Which airplane are you referring to?

A The B-52.

Q What makes an airplane obsolete?

A Oh, principally speed today.

Q Speed. How fast will the helicopter go?

A Oh, they are very slow.

Q Are they still used today?

A Oh, yes.

Q Are they obsolete?

A No, they even have one at Grand Forks for the purpose of supervising the missile site.

Q How about some of the prop planes, spotter planes, in Vietnam; are they obsolete?

A No, but if you were supplying fuel for them you could do it with a bucket.

Q That is not true with respect to the B-52, though, is it?

A Oh, no.

Q Did you know that the plans for the B-52 are that they are going to increase in the Grand Forks area? Did you know that?

A No, and our deliveries have started back down in the last couple of years.

Q Do you know what the projection is for the future?

A No.

Q You don't know. When you say that the B-52's have become obsolete, can you describe the research that you have gone into to determine this fact?

A I don't attempt to qualify myself as an expert on aerodynamics, but I, as a contractor to the Air Force, have occasion to get the opinions of the best people in the Air Force

I am able to, and they tell me the old girl has about had it.

Q What are the names of these people that you have mentioned?

A The names of these people? Well, a general named York, who—

Q What is his function?

A He is down in Texas at the present time. He was one of the Doolittle Raiders over Tokyo.

Q And what is his position with the Air Force?

A I think it is pretty much administrative.

Q What does he administer?

A I don't know at the present time?

Q He has nothing to do with the Fuel Supply Section of the Air Force, does he?

A No, I think he is in general administration.

Q Do you have any views of any people other than those in general administration?

A Yes, my conversations with pilots at local clubs and such.

Q So your information is based on conversations more of the bar room type?

A Well, in casual conversations with those people, yes.

Q I see. Are you also of the same opinion as Mr. Clack, that the B-70 will be a chemical fuel bomber?

THE COURT: You mean Mr. Davis?

MR. RAMSEY: As Mr. Davis, excuse me.

A The B-70 uses a highly sophisticated type of fuel, I understand, called JP-6, which I am not sure our facility is designed to store and handle. I think it has a vapor pressure.

Q Do you know what JP stands for?

A The same as JI-4, I presume, jet propulsion.

Q Not jet petroleum?

A Either jet propulsion or jet petroleum.

Q But you don't agree with Mr. Davis, that it is a chemical bomber?

A It is a highly sophisticated fuel that has additives that our present fuel does not have, and I am inclined to be of the opinion that with our present plants, without being able to handle high vapor pressures, probably would be unsatisfactory.

Q Did you know that they have started using JP-5 for the B-70 now?

A No, I don't know that, but the B-70 originally was not supposed to.

Q Have you made any research into the area

of whether or not your terminal facility could be adjusted for the use of any new fuels that might come along, if some did?

A Sure, you can redesign anything.

Q But have you made any research in an attempt to determine this?

A No. I do know they built two B-70's and they lost one of them.

Moreover, apart from the complete vagueness and conjectural nature of the taxpayer's basis for allegedly anticipating nonrenewal because of the use of missiles, it is of utmost importance to note that nowhere does taxpayer show basis for estimating (with reasonable certainty, or upon any other basis) over what period, assuming that there was reason to believe that the bombers would be phased out, the phasing out would take place or, therefore, as of what time it could anticipate that its facility would no longer be in profitable use. All military aircraft are in the process of obsolescing from the moment they are put into use and their successors are always on the drawing board. It is of no use then to show a basis for a reasonable belief that the B-52's in particular would, in reasonable anticipation, go into disuse at some unknown time in the future. It is the taxpayer's burden not only to show a basis for belief that phasing out would occur, or was occurring, but a basis for a reasonably certain belief that the phasing out would occur over some particular period

of time and that, as a result, taxpayer's facility would not be needed beyond a given point of time. Cf. *Lassen Lumber & Box Co.* v. *Blair, supra.* In this connection, it is necessary to take into account any continued period of use for existing B-52's, even after manufacture of new ones was discontinued for one reason or another. Further, the taxpayer must show not only that the facility would have no further use to the Government in connection with B-52's, but also that it was unlikely to have any continued usefulness in connection with fuel storage for other types of aircraft. None of these essential facts were developed by taxpayer at trial and he has, therefore, on this ground alone, clearly failed, as a matter of law, to carry his burden of proof. Hence, on this record, the District Court would have been clearly erroneous in finding anything other than that the 20-year useful life adopted by the Commissioner must stand. Cf. *Helvering* v. *Gowran,* 302 U.S. 238, 245-247, rehearing denied, 302 U.S. 781.

CONCLUSION

The judgment of the District Court should be affirmed. However, if this Court does not agree that, looking to the facts existing in 1960, the taxpayer has failed, as a matter of law, to adduce evidence sufficient to support a finding of a useful life of less than 20 years, then the case should be remanded for findings on the basis of the stated evidence.

Respectively submitted,

MITCHELL ROGOVIN,
Assistant Attorney General.
LEE A. JACKSON,
WILLIAM FRIEDLANDER,
JEANINE JACOBS,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

Of Counsel:
SMITHMOORE P. MYERS,
United States Attorney.

MAY, 1968.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: This _____ day of _____, 1968.

_____
United States Attorney

APPENDIX

Internal Revenue Code of 1954:

SEC. 167. DEPRECIATION.

(a) *General Rule.*—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

(1) of property used in the trade or business, or

(2) of property held for the production of income.

(b) *Use of Certain Methods and Rates.*—For taxable years ending after December 31, 1953, the term "reasonable allowance" as used in subsection (a) shall include (but shall not be limited to) an allowance computed in accordance with regulations prescribed by the Secretary or his delegate, under any of the following methods:

(1) the straight line method,

(2) the declining balance method, using a rate not exceeding twice the rate which would have been used had the annual allowance been computed under the method described in paragraph (1),

(3) the sum of the years-digits method, and

(4) any other consistent method productive of an annual allowance which, when added to all allowances for the period commencing with the taxpayer's use of the property and in-

cluding the taxable year, does not, during the first two-thirds of the useful life of the property, exceed the total of such allowances which would have been used had such allowances been computed under the method described in paragraph (2).

Nothing in this subsection shall be construed to limit or reduce an allowance otherwise allowable under subsection (a).

(c) *Limitations on Use of Certain Methods and Rates.*—Paragraphs (2), (3), and (4) of subsection (b) shall apply only in the case of property (other than intangible property) described in subsection (a) with a useful life of 3 years or more—

(1) the construction, reconstruction, or erection of which is completed after December 31, 1953, and then only to that portion of the basis which is properly attributable to such construction, reconstruction, or erection after December 31, 1953, or

(2) acquired after December 31, 1953, if the original use of such property commences with the taxpayer and commences after such date.

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(26 U.S.C. 1964 ed., Sec. 167.)

Treasury Regulations on Income Tax (1954 Code):

Sec. 1.167(a)-1 *Depreciation in general.*

(a) *Reasonable allowance.* Section 167(a) pro-

vides that a reasonable allowance for the exhaustion, wear and tear, and obsolescence of property used in the trade or business or of property held by the taxpayer for the production of income shall be allowed as a depreciation deduction. The allowance is that amount which should be set aside for the taxable year in accordance with a reasonably consistent plan (not necessarily at a uniform rate), so that the aggregate of the amounts set aside, plus the salvage value, will, at the end of the estimated useful life of the depreciable property, equal the cost or other basis of the property as provided in section 167(g) and §1.167(g)-1. An asset shall not be depreciated below a reasonable salvage value under any method of computing depreciation. However, see section 167(f) and §1.167(f)-1 for rules which permit a reduction in the amount of salvage value to be taken into account for certain personal property acquired after October 16, 1962. See also paragraph (c) of this section for definition of salvage. The allowance shall not reflect amounts representing a mere reduction in market value. See section 179 and §1.179-1 for a further description of the term "reasonable allowance."

(b) *Useful life.* For the purpose of section 167 the estimated useful life of an asset is not necessarily the useful life inherent in the asset but is the period over which the asset may reasonably be expected to be useful to the taxpayer in his trade or business or in the production of his income. This period shall be determined by reference to his experience with similar property taking into account present conditions and probable future developments. Some of the factors to be considered in determining this period are (1) wear and tear and decay or decline from

natural causes, (2) the normal progress of the art, economic changes, inventions, and current developments within the industry and the taxpayer's trade or business, (3) the climatic and other local conditions peculiar to the taxpayer's trade or business, and (4) the taxpayer's policy as to repairs, renewals, and replacements. Salvage value is not a factor for the purpose of determining useful life. If the taxpayer's experience is inadequate, the general experience in the industry may be used until such time as the taxpayer's own experience forms an adequate basis for making the determination. The estimated remaining useful life may be subject to modification by reason of conditions known to exist at the end of the taxable year and shall be redetermined when necessary regardless of the method of computing depreciation. However, estimated remaining useful life shall be redetermined only when the change in the useful life is significant and there is a clear and convincing basis for the redetermination. For rules covering agreements with respect to useful life, see section 167(d) and §1.167(d)-1.

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(26 C.F.R., Sec. 1.167(a)-1.)

Sec. 1.167(b)-0 *Methods of computing depreciation.*

(a) *In general.* Any reasonable and consistently applied method of computing depreciation may be used or continued in use under section 167. Regardless of the method used in computing depreciation, deductions for depreciation shall not exceed such amounts as may be necessary to recover the unrecovered cost or other

basis less salvage during the remaining useful life of the property. The reasonableness of any claim for depreciation shall be determined upon the basis of conditions known to exist at the end of the period for which the return is made. It is the responsibility of the taxpayer to establish the reasonableness of the deduction for depreciation claimed. Generally, depreciation deductions so claimed will be changed only where there is a clear and convincing basis for a change.

(b) *Certain methods.* Methods previously found adequate to produce a reasonable allowance under the Internal Revenue Code of 1939 or prior revenue laws will, if used consistently by the taxpayer, continue to be acceptable under section 167(a). Examples of such methods which continue to be acceptable are the straight line method, the declining balance method with the rate limited to 150 percent of the applicable straight line rate, and under appropriate circumstances, the unit of production method. The methods described in section 167(b) and §§ 1.167(b)-1, 1.167(b)-2, 1.167(b)-3, and 1.167(b)-4 shall be deemed to produce a reasonable allowance for depreciation except as limited under section 167(c) and §1.167(c)-1. See also §1.167(e)-1 for rules relating to change in method of computing depreciation.

(c) *Application of methods.* In the case of item accounts, any method which results in a reasonable allowance for depreciation may be selected for each item of property, but such method must thereafter be applied consistently to that particular item. In the case of group, classified, or composite accounts, any method may be selected for each account. Such method

must be applied to that particular account consistently thereafter but need not necessarily be applied to acquisitions of similar property in the same or subsequent years, provided such acquisitions are set up in separate accounts. See, however, §1.167(e)-1 and section 446 and the regulations thereunder, for rules relating to changes in the method of computing depreciation, and §1.167(c)-1 for restriction on the use of certain methods. See also §1.167(a)-7 for definition of account.

(26 C.F.R., Sec. 1.167(b)-0.)

Sec. 1.167(b)-2 *Declining balance method.*

(a) *Application of method.* Under the declining balance method a uniform rate is applied each year to the unrecovered cost or other basis of the property. The unrecovered cost or other basis is the basis provided by section 167(g), adjusted for depreciation previously allowed or allowable, and for all other adjustments provided by section 1016 and other applicable provisions of law. The declining balance rate may be determined without resort to formula. Such rate determined under section 167(b)(2) shall not exceed twice the appropriate straight line rate computed without adjustment for salvage. While salvage is not taken into account in determining the annual allowances under this method, in no

event shall an asset (or an account) be depreciated below a reasonable salvage value. However, see section 167(f) and § 1.167(f)-1 for rules which permit a reduction in the amount of salvage value to be taken into account for certain personal property acquired after October 16, 1962. Also, see section 167(c) and § 1.167(c)-1 for restrictions on the use of the declining balance method.

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(26 C.F.R., Sec. 1.167(b)-2.)